

BUDGET LETTER

	NUMBER: 03-18
SUBJECT: 2004-05 BUDGET POLICY	DATE ISSUED: July 8, 2003
REFERENCES: BL 03-05	SUPERSEDES: BL 02-20

TO: Agency Secretaries
Department Directors
Departmental Budget Officers
Departmental Accounting Officers
Department of Finance Budget Staff

FROM: DEPARTMENT OF FINANCE

This Budget Letter (BL) sets forth the Governor's policy direction for preparation of his 2004-05 Budget. As a reminder, BL 03-05, issued March 26, 2003, outlines the technical and procedural requirements for preparation of the 2004-05 Budget. BL 03-05 describes the framework for the completion and submission of proposed baseline/current services departmental budgets.

Current Year Deficiencies

Despite the major reductions to programs proposed for the 2003-04 Budget, given the current fiscal environment, departments are advised that current year State Operations' deficiencies will not be approved. Departments must absorb any increased costs. The Department of Finance (Finance) will only consider deficiencies for extraordinary circumstances. Consult with your Finance Program Budget Manager before submitting any deficiency requests.

Budget Change Proposals

Unless legislative steps are taken to address the budget's structural imbalance, currently authorized expenditures and statutorily required expenditure adjustments will exceed available resources in 2004-05. Therefore, there will be no discretionary funds available from any fund source for new initiatives or program expansion.

Agencies and departments should not submit requests for new programs or for expansion of existing programs. This includes information technology (IT) activities. During this time, the State needs to focus on only its most essential IT projects as well as the security of IT operations. Budget Change Proposals (BCPs) to fund new initiatives or program expansions will not be reviewed (unless they include revenue-generating proposals that would make them cost-beneficial), and will be returned to the requesting department or Agency. BCPs to fund workload increases or costs of legislation must be accompanied by commensurate proposed reductions in other existing programs. To avoid unnecessary workload, agencies are encouraged to discuss departments' budget change concepts with the appropriate Finance Program Budget Manager, prior to fully developing BCPs.

Addressing the 2004-05 Funding Gap

After Budget enactment, the Legislature has been asked to spend the balance of the legislative session to address the structural issues that, if left unresolved, will put future budgets out of balance and threaten the future prosperity of our State's citizens. Based on the May Revision projections, absent legislative

corrective actions, the 2004-05 General Fund funding gap is estimated at \$7.9 billion. The ultimate funding gap will change depending on the final Budget and the legislative actions to address the structural gap. Some measures may require Constitutional or statutory changes that could be placed before the electorate.

Since the timing and final outcome of such actions are currently unknown, the Administration must collectively make further spending reductions in 2004-05 to bring ongoing expenditures in line with ongoing resources. **Consequently, Agencies and departments must be prepared to submit expenditure reduction plans similar to last year for both state operations and local assistance.** These reduction plans apply to General Fund and selected non-General funds (departments affected by these non-General funds will be separately notified by your Finance analyst).

Reductions for the 2004-05 Budget will continue to be complex, require the elimination of programs or layoff of employees, and require certain level of lead time both for development and implementation. Acknowledging that significant programmatic impacts have been incurred pursuant to position reductions, prior unallocated reductions, and other budget reductions, Agencies and departments must propose specific reductions that incorporate one or more of the following: (1) the repeal of statutorily required activities or programs; (2) the elimination of discretionary programs; (3) program consolidation; (4) the reorganization of Agencies, departments, boards, commissions, and offices (proposed reorganizations that cross Agency jurisdictions must be submitted jointly by the affected Agencies); and (5) restructuring program responsibilities between the State and local governmental entities. Detailed instructions will be issued later to formalize the reduction plan submission process.

Proposed Statutory Changes

Pursuant to Government Code Section 13308, Finance must provide to the Legislature on or before February 1 of each year, all proposed statutory changes, as prepared by the Legislative Counsel, necessary to implement the Governor's Budget. Therefore, all Budget Change or Reduction Proposals that require statutory changes also must include a copy of the proposed legislation. Finance will submit the approved language to the Legislative Counsel.

Comprehensive Budget Development Process

The Government Code and Budget Act require the Governor's Budget development process to be as comprehensive as possible, and any subsequent adjustments may only be made to meet critical and unanticipated needs. Further, the January Budget is to include all policy proposals being made for the ensuing fiscal year. Spring Finance Letters, due to the Legislature no later than April 1, should be used only for (a) updating those proposals made in January or (b) submitting any new critical proposals that cannot be delayed until the upcoming fall budget process without serious consequences. The May Revision changes to the Governor's Budget are due to the Legislature no later than May 14 and will encompass only traditional enrollment, caseload, and population adjustments and any necessary budget balancing proposals.

If you have any questions, please contact your Finance budget analyst.

/s/ Steve Peace

STEVE PEACE
Director